

# In the Supreme Court of the United States

OCTOBER TERM, 1924

BLAKELY D. McCAUGHN, COLLECTOR OF INTERNAL REVENUE, PETITIONER v. CHARLES H. LUDINGTON	}	No. —
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## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF

The Solicitor General, on behalf of Blakely D. McCaughn, Collector of Internal Revenue for the First District of Pennsylvania, applies for a writ of certiorari to review the judgment of the United States Circuit Court of Appeals for the Third Circuit, entered on October 1, 1924, reversing the judgment of the District Court of the United States for the Eastern District of Pennsylvania.

### STATEMENT OF THE CASE

Charles H. Ludington, the respondent, prior to March 1, 1913, purchased 490 shares of the first preferred stock of the United Gas & Electric Corporation and 60 shares of the 6% cumulative preferred stock of the American Cities Company at a cost of \$32,500. The fair market value of said shares as of March 1,

1913, was \$37,050. In 1919 respondent sold these shares of stock for the sum of \$3,866.91, thereby sustaining a loss of \$28,633.09.

In making his income tax return for the year 1919 respondent claimed as a deductible loss the sum of \$33,183.09, being the difference between the March 1, 1913, value of these stocks, \$37,050, and the sale price of \$3,866.91. Upon an audit of his return the Commissioner of Internal Revenue determined the amount of the loss as the difference between the cost, \$32,500, and the sale price, \$3,866.91, or a loss of \$28,633.09. This resulted in increasing the tax of the respondent for said year by the sum of \$3,094. This amount was paid under protest, whereupon this action was instituted for its recovery with interest.

The United States District Court for the Eastern District of Pennsylvania gave judgment for the defendant, and on writ of error the Circuit Court of Appeals for the Third Circuit reversed the judgment and directed a new trial.

Candor requires me to say that the judgment of the Circuit Court of Appeals was not in form final. Although technically it did not terminate the litigation because it was necessary that certain perfunctory proceedings should thereafter take place in the trial court, that judgment was, however, definitive as to the question of law involved. And I agree with the view expressed by counsel for the respondent in the memorandum they have filed in support of this petition, that this is a case in which the Court may very properly disregard the general rule and exercise

its undoubted power of granting a writ of certiorari before final judgment, to the end that the construction by this court of an important provision of internal revenue law may not be delayed pending purely formal proceedings in the courts below, and that the Government and the taxpayer may be spared the needless expense which a protraction of the litigation would cause. In addition, as hereinafter pointed out, there is now on the docket of this Court a case which presents another aspect of the question involved in the case at bar. If the Court should grant the writ at this stage of the litigation, it would be possible to place all phases of the question before it at the same time and not by piecemeal.

#### QUESTION PRESENTED

Where property acquired before March 1, 1913, at less than its value on that date was sold in 1919 for less than cost, may the taxpayer, under the Revenue Act of 1918, deduct, as loss, the difference between the selling price and the March 1, 1913, value, which amount was greater than the *actual* loss sustained, or is he limited to *actual* loss?

#### REVENUE ACT OF 1918

SEC. 202. (a) That for the purpose of ascertaining the gain derived *or loss sustained* from the sale or other disposition of property, real, personal, or mixed, the basis shall be—

(1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date \* \* \*. (40 Stat. 1060.) (Italics ours.)

## REASONS FOR GRANTING THE PETITION

1. The question involved is of general importance to the Government and to the public because of its far-reaching effect. Many cases are pending in the courts involving the same question and hundreds of cases have been settled by the Commissioner of Internal Revenue upon the basis of disallowing a loss, where the actual selling price was greater than the cost of property acquired prior to March 1, 1913. With the possible exception of the cases with respect to stock dividends, the decision of the question in issue will possibly affect more taxpayers and involve larger amounts of revenue than any tax decision within the last decade.

2. The construction placed upon the Act by the Circuit Court of Appeals with regard to "losses" is inconsistent with the construction placed upon similar language of the Revenue Act of 1916 with respect to "gains" in *Goodrich v. Edwards*, 255 U. S. 527, and *Walsh v. Brewster*, 255 U. S. 536.

3. There is now pending in this Court on appeal from the United States Court of Claims the case of *United States v. Harriett R. Flannery et al.*, No. 527 on the docket for the present term, in which another aspect of this same question is involved, namely, the sale by a taxpayer in the year 1919 of shares of stock owned by him on March 1, 1913, at less than the fair market price or value thereof on said date but at more than the anterior cost thereof. In the instant case there is involved the other aspect of the question, namely, sale by a taxpayer in 1919 of shares of

stock owned by him on March 1, 1913, at less than the fair market price or value thereof on said date as well as at less than the anterior cost thereof. Petitioner considers it desirable that this petition be granted in order that the instant case may be heard by this Court in connection with the *Flannery case*, so that there may be a complete adjudication by the Court of all phases of this important question.

As stated above, the respondent has filed a memorandum in which he joins the petitioner in requesting that the writ of certiorari be issued.

JAMES M. BECK,  
*Solicitor General.*

NOVEMBER, 1924.

### BRIEF IN SUPPORT OF PETITION

The Revenue Act of 1916 with respect to gains and losses contained practically the same language as the Act of 1918, involved in the case at bar. That portion of the provisions of the Act of 1916 which related to gains came before this Court for construction in *Goodrich v. Edwards*, 255 U. S. 527, and *Walsh v. Brewster*, 255 U. S. 536. This Court held that "gains" as used in those provisions meant *actual* gains; that is to say, the difference between the cost of the property to the taxpayer and the price at which he sold the same. In reaching this conclusion, this Court said in *Goodrich v. Edwards*, *supra*:

It is thus very plain that the statute imposes the income tax on the proceeds of the sale of personal property to the extent only that *gains* are derived therefrom by the vendor, and we therefore agree with the Solicitor General that since no gain was realized on this investment by the plaintiff in error no tax should have been assessed against him.

Section 2 (c) is applicable only where a gain over the original capital investment has been realized after March 1, 1913, from a sale or other disposition of property. (255 U. S. 535.)

Petitioner submits that it is very evident that Congress intended to establish a uniform, harmonious, and consistent basis for ascertaining gains

derived and losses sustained in computing net income for purposes of taxation in each of these Revenue Acts. It is obvious therefore that the holding of this Court in the cases of *Goodrich v. Edwards* and *Walsh v. Brewster*, *supra*, that the language of the Act of 1916 as applied to gains means only those *actual* gains which constitute the difference between cost and selling price necessarily requires a similar construction of this language with respect to deductible losses. That is to say, it was intended to prevent the deduction of anything except *actual* losses, viz, the difference between selling price and cost of the property sold to the taxpayer. Any other holding would make practically the same language mean one thing with respect to gains derived and another thing with respect to losses sustained, thereby nullifying the plain intent of Congress.

In view of the inconsistency which exists between the decision of the Circuit Court of Appeals in the present case and the holding of this Court in *Goodrich v. Edwards* and *Walsh v. Brewster* and of the far-reaching effect of the question involved upon the Government and the public generally, it is respectfully submitted that the petition for writ of certiorari should be granted.

JAMES M. BECK,  
*Solicitor General.*

NOVEMBER, 1924.